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The Next-Gen DVD Format War: Still Bloody

by J. P. Gownder
for Strategy Professionals



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Blu-ray Must Drop Hardware Prices Quickly To Beat HD-DVD

by J. P. Gownder

with Brad Holmes, Ellen Daley, James L. McQuivey, Paul Jackson, and Remy Fiorentino

EXECUTIVE SUMMARY

Forrester predicted in 2005 that Blu-ray would eventually win a hard-fought victory over HD-DVD in the next-generation DVD format war. Today, Forrester believes that Blu-ray remains in a better position than HD-DVD — but that Blu-ray strategists need to alter course. Blu-ray's failure to land a knock-out blow means that the format war will continue for at least 18 more months. Blu-ray's content advantages are somewhat diminished since the recent decision by Paramount to commit exclusively to HD-DVD. And HD-DVD hardware prices have dropped directly into consumers' preferred price range, according to Forrester's Technographics' survey data. Weakened by these developments, Blu-ray needs to offer a viable hardware model at the \$250 price point by Christmas 2007. The Blu-ray camp must also stave off further studio defections, and employ more aggressive promotional tactics to counter HD-DVD's recent momentum. Failure to alter strategy would open up Blu-ray to a possible upset defeat at the hands of HD-DVD.

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NOTES & RESOURCES

Forrester interviewed the Blu-ray Disc Association, the HD-DVD Association, LG Electronics, Philips, Sony, Toshiba America, and Warner Bros. Entertainment.

Related Research Documents

["CES 2007: The End Of The High-Definition DVD Format War?"](#)

January 16, 2007

["Blu-ray Disc Will Still Beat HD-DVD"](#)

October 5, 2006

["Blu-ray Will Win A Pyrrhic Victory Over HD-DVD"](#)

October 19, 2005

BLU-RAY FAILED TO LAND THE KNOCK-OUT PUNCH

In October 2005, Forrester predicted that Blu-ray would beat out HD-DVD as the next-generation DVD standard, but that this victory would come at great cost.¹ Two years later, however, the format war has hit an impasse because Blu-ray has thus far failed to land a knock-out punch:

- **Sony Electronics' PlayStation 3 (PS3) launch didn't live up to early expectations.** Blu-ray's strategic advantage depended in part on the expectation that millions of PS3 owners would be able to play the format's discs. Sony's PS3 launch wound up being a borderline disaster: Production glitches, a delayed European launch, a lack of gaming titles, an exceptionally high price point, mixed reviews, and unexpected competition from Nintendo's Wii all conspired to give the platform a problematic start. Recent sales have been better, but the PS3's woes hurt Blu-ray by diminishing its expected installed base of hardware.²
- **High-definition services remain poorly understood and under-subscribed.** Consumers have struggled to understand the entire realm of high-definition video. As of Q4 2006, only 15% of US households owned an HDTV. And among these HDTV owners, only 53% subscribed to high-definition cable services.³ This lack of services adoption is telling: If HDTV owners haven't embraced, or worse, don't grok the value of high-definition television programming, how likely are they to trade in their standard-format DVD players for the next generation?
- **Many consumers are not aware of next-generation DVD solutions.** More than half of all US households haven't heard of either next-generation format (see Figure 1). Among HDTV-owning households, nearly half haven't heard of Blu-ray, and more than a third haven't heard of HD-DVD.⁴ Less than a fifth of HDTV-owning households report having seen a next-generation player. Consumer awareness, exposure, and ownership remain stunted.
- **The HD-DVD camp's strategists have been aggressive on pricing . . .** Partisans of HD-DVD have leveraged a wide variety of tactics to stave off a Blu-ray victory — in particular, promotions for free discs when buying HD-DVD hardware (currently eight free discs) and low hardware prices (half the price of the least expensive Blu-ray player).⁵
- **. . . and on deal-making.** The HD-DVD camp enticed Paramount to become HD-DVD exclusive in its high-definition releases, having previously supported both formats. This defection means that Paramount and Universal Studios are both HD-DVD exclusive.⁶ Also, Dreamworks Animation, which hadn't released high-definition movies, joined the HD-DVD camp. While these studio relationships were costly (\$150 million in incentives were paid, according to many sources), they changed the content dynamics enough to rob Blu-ray of momentum.

Figure 1 Awareness And Penetration Remain Tepid For Both Formats

“HD-DVD and Blu-ray are two different formats for the next generation of DVDs. These DVDs produce a true high-definition picture when connected to HDTV. How familiar are you with HD-DVD players?”

Next-generation DVD solution	HDTV-owning households		All households*	
	Blu-ray	HD-DVD	Blu-ray	HD-DVD
I never heard of them before this survey	49%	37%	67%	54%
I have heard of them but don't know what they are	17%	15%	16%	19%
I know what they are but I have never seen one	18%	22%	12%	17%
I have seen one but don't own one	14%	21%	5%	9%
I own one	1%	6%	0%	1%

Base: 717 US households with HDTV
*Base: 5,005 US households

Source: Forrester's NACTAS Q4 2006 Survey
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Source: Forrester Research, Inc.

THE FORMAT WAR WILL REMAIN DEADLOCKED FOR THE NEXT 18 MONTHS

Unfortunately for the consumer, the format war shows no signs of abating in the next year and a half.

Strategists In Each Coalition Are Still Going Head-To-Head . . .

Strategists on both sides of the format war express strong continued support for their solutions, and neither of the opposing camps has publicly backed down in the slightest:

- **Microsoft, Toshiba America, and Universal Studios remain steadfast.** These HD-DVD champions point out that the market remains truly in its infancy in terms of volume and penetration. They believe that the lower prices of their hardware solutions, and cheaper production costs for discs, will eventually help HD-DVD prevail. At worst, they envisage an industry akin to the videogame console market, where different format players coexist in the market, many best-sellers are available across platforms, but some titles can only be enjoyed in particular formats. Having added Paramount to their coalition, they believe that the content gap is closing, and that the release of “Transformers” on HD-DVD in late 2007 will drive HD-DVD hardware sales.⁷
- **The much larger Blu-ray coalition has joined HD-DVD in playing the promotion game.** Case in point? The Blu-ray Disc Association has countered lower HD-DVD hardware prices with a content offer — receive five free discs when you buy a new Blu-ray player.⁸ Disney is now launching an 18-city road show to increase consumer awareness of the Blu-ray format.⁹ And Sony now offers two Blu-ray disc players for \$499: the BDP-S300 pure player and a version of

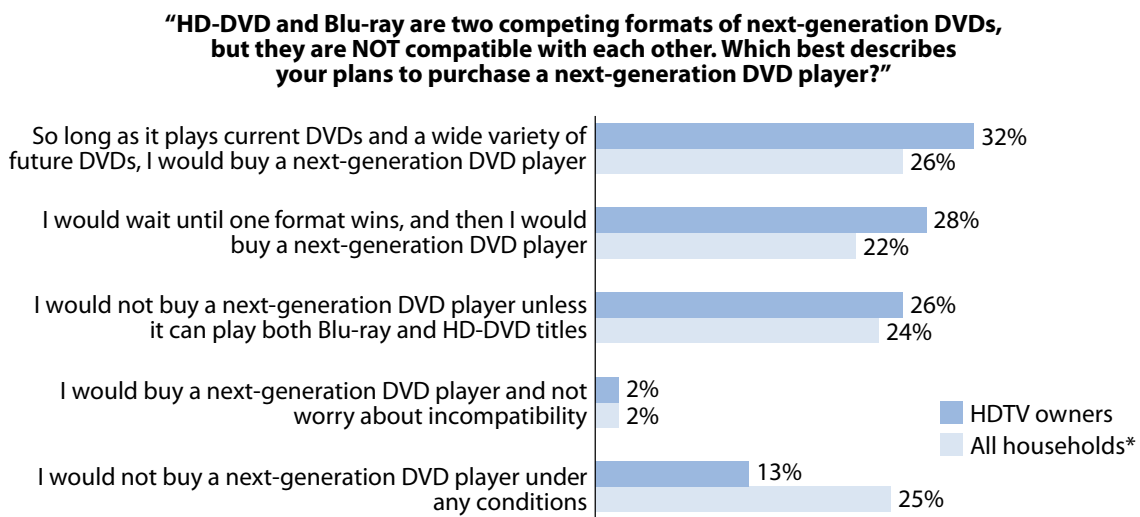
the PS3 following a \$100 price cut.¹⁰ Blu-ray strategists are now charging ahead by employing aggressive promotional tactics, complementing their strategy of having the broadest coalition of hardware and content providers. Blu-ray partisans still believe this broad coalition and what they believe is a technically superior format will carry them to victory.

... While Consumers' Halfhearted Next-Generation DVD Preferences Promote Stalemate

With both formats available in the market, consumers could pick a format war winner once and for all. But Forrester's consumer survey data — particularly that from the first wave of likely buyers, HDTV owners — suggests they remain gridlocked as:

- **Only one third of HDTV owners are willing to make a format choice.** Only 32% of HDTV owners say that “so long as it plays my current DVDs and a wide variety of future DVDs, I would buy a next-generation DVD player” (see Figure 2). And practically none — only 2% — say “I would buy a next-generation DVD player and not worry about incompatibility.”
- **More than one quarter of HDTV owners say they will “wait until one format wins.”** HDTV owners feel more strongly about waiting for resolution before buying than do average households by a score of 28% to 22%.
- **Dual-format players appeal to consumers as much as an end to the format war.** Fully 26% of HDTV owners say they “would not buy a next-generation DVD player unless it can play both Blu-ray and HD-DVD titles.” LG Electronics, with its Super Blu product, and Samsung, which has announced a dual-format player for fall 2007, will be beneficiaries of consumers' distaste for the format war.

Figure 2 Dual-Format Players Are As Appealing As An End To The Format War



Base: 717 US households with HDTV
*Base: 5,005 US households

Source: Forrester's NACTAS Q4 2006 Survey

43013

Source: Forrester Research, Inc.

BLU-RAY'S STRATEGIC ADVANTAGES COULD BE UNDONE BY PRICE — AND CONTENT

The pyrrhic victory Forrester predicted two years ago is in question. And when a resolution to the war does come, the costs may outweigh the benefits for all industry participants.

Consumer Price Proclivities Favor HD-DVD . . .

Consumers still think of next-generation DVD players, and the discs themselves, in the same way they think of standard-format DVD players and discs — as commodities. Consumers:

- **Want next-generation DVD players to cost around \$200.** Forrester asked consumers, “what is the most you would be willing to pay for a new HD-DVD or Blu-ray player?” The typical HDTV owner today wasn’t willing to pay more than \$204 on average (see Figure 3). Even among those HDTV owners who are aware of next-generation DVD players, their preferred price point is merely \$228 on average. Mass adoption of players will remain elusive until prices reach this range — and Blu-ray isn’t even in the vicinity.¹¹
- **Care only somewhat about disc capacity and downloading.** Holding a full season of a TV show on one disc appeals to 41% of buyers, while 33% are interested in downloading and burning (see Figure 4). Blu-ray’s capacity advantages might find interest among some consumer buyers.
- **Don’t care about videogame players or interactivity.** Buyers aren’t necessarily choosing their high-definition solution based on its integration with an XBox 360 (HD-DVD) or PS3 (Blu-ray). And HD-DVD’s interactive online features won’t drive adoption.
- **Care much less about back-catalog releases versus new content.** During the VHS to DVD transition, consumers put aside entire libraries of old tapes in favor of DVD versions. This back-catalog purchasing will not happen in the next-generation DVD market (see Figure 5). Back-catalog releases, such as Fox’s August 2007 release of “must have” older titles, are therefore less important — helping Blu-ray only among a small segment of consumers.¹²

Figure 3 Consumer Price Perceptions Of Next-Generation DVD Players Lag Market Prices

“What is the most you would be willing to pay for a new HD-DVD or Blu-ray player?”

All HDTV owners who might be interested in paying for a next-generation DVD player	\$204
HDTV owners who are not aware of next-generation DVD players*	\$174
HDTV owners who are aware of next-generation DVD players†	\$228

Base: 553 US households that are interested in paying for an HD-DVD or Blu-ray player and own an HDTV set

*Base: 252 US households with HDTV that are not aware of HD-DVD that would pay for HD-DVD

†Base: 301 US households with HDTV that are aware of HD-DVD that would pay for HD-DVD

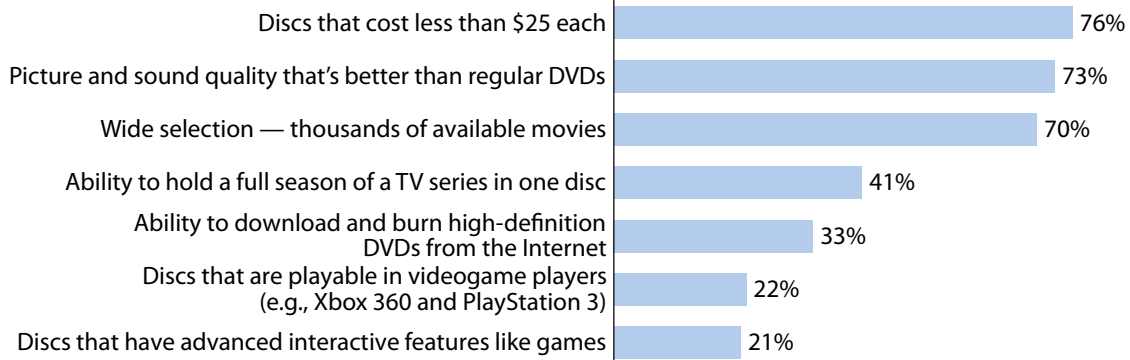
Source: Forrester’s NACTAS Q4 2006 Survey

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Source: Forrester Research, Inc.

Figure 4 Price, Quality, And Selection Are Top Qualities In Next-Generation DVDs

“How important will each of the following features be when buying a next-generation DVD player?”



Base: 717 US households with HDTV

Source: Forrester’s NACTAS Q4 2006 Survey

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Source: Forrester Research, Inc.

Figure 5 Consumers Are Overwhelmingly Resistant To DVD Replacement

“If high-definition DVD movies cost \$25 each, how many of your current DVDs would you replace with new DVDs in a high-definition format?”

	HDTV owners	Aware of or own a next-generation DVD player*	All households†
None	87%	87%	91%
1	1%	2%	1%
2	3%	3%	2%
3	2%	2%	1%
4 to 5	3%	3%	2%
6 to 9	1%	1%	1%
10 or more	3%	3%	1%

Base: 717 US households with HDTV
*Base: 1,363 US households aware of HD-DVD
†Base: 5,005 US households

Source: Forrester’s NACTAS Q4 2006 Survey

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Source: Forrester Research, Inc.

... And They Want The Format That Will Give The Most Content

Consumers tell us they care a lot about disc price, video quality, and available content — these three criteria form the top tier of buyer preferences. Disc prices and video quality arguably show little difference between the two formats. So content is where differentiation is happening. Since available content is determined in large part by studio support, the alliances with studios are so critical to strategists.

- **Today, available content favors Blu-ray — but less than it did in the past.** Blu-ray holds an advantage in this category, but one that has been diminished by the recent defection of Paramount and Dreamworks’ decision to align with HD-DVD.
- **The established base of consumers favors Blu-ray — for now.** Blu-ray enjoys an advantage on this dimension in light of the Blockbuster experience. Blockbuster announced its intention to only stock Blu-ray in 1,700 retail outlets in June 2007.¹³ The decision was based on real-world behavior — in trial at 250 stores, renters chose Blu-ray over HD-DVD by 70% to 30%, most of which was likely driven by PS3 users. But the price of hardware affects this metric, and rapidly. Christmas 2007 will be an important watershed for hardware.

RECOMMENDATIONS

TO WIN, BLU-RAY PARTISANS MUST DROP THEIR HARDWARE PRICES

Forrester has long predicted that Blu-ray will win. Its strategic advantages in content and the established base of players, plus its huge coalition of hardware and content providers, continue to give the format an edge over HD-DVD. But aggressive hardware prices for HD-DVD players threaten to undo the Blu-ray strategy. To succeed:

- **Blu-ray's hardware makers must continue to rapidly march down the price ladder.** The Blu-ray camp needs to offer a widely available, functionally satisfactory hardware option for \$250 or less by Christmas 2007. Failing to do so would jeopardize Blu-ray's superior position in the market, particularly if consumers snap up HD-DVD players for under \$200 — as Forrester's data indicates they want.
- **The Blu-ray forces should triple their promotional efforts.** To ensure a 2009 victory, other Blu-ray consortium members should follow Disney's lead and develop contextual road shows to educate the market about Blu-ray. They should also offer much more aggressive promotional incentives for purchasing a Blu-ray player at the time the consumer purchases his or her HDTV set. The existing five-free-discs offer comes from too limiting a list of titles. A movie like "300" would be better.
- **Blu-ray needs to stave off further studio defections.** Blu-ray's advantage in content remains critical, but a defection from another studio would throw the entire competition into a price gain — which Blu-ray isn't poised to win at the moment. Incentives like those given to Paramount are fair tactics for strategists involved in a format war.
- **Dual-format disc player makers must sneak into the market quickly.** The benefits of a dual-format player run out when the price of buying both a Blu-ray player plus an HD-DVD player drops below \$500. LG Electronics' Super Blu, exceptionally overpriced at \$1,299, needs to drop significantly. Samsung's autumn release must come in below \$500 to capture the market's attention. By the end of 2007, these players should retail for \$400 or less to capture share.

SUPPLEMENTAL MATERIAL

Companies Interviewed For This Document

Blu-ray Disc Association	Sony
HD-DVD Association	Toshiba America
LG Electronics	Warner Bros. Entertainment
Philips	

ENDNOTES

- ¹ Forrester predicted that Blu-ray would prevail early in the format war's history. See the October 19, 2005, "[Blu-Ray Will Win A Pyrrhic Victory Over HD-DVD](#)" report, and see the October 5, 2006, "[Blu-Ray Disc Will Still Beat HD-DVD](#)" report.
- ² Sony PlayStation's problems were clear to Forrester as early as November 2006. See the November 14, 2006, "[The Dawn Of The Next Videogame Console War](#)" report. Recent news suggests that Sony might be back on track, globally at least, to meet its sales goals, following a price cut on one model. Source: Scott Hillis, "GAMES EXPO-INTERVIEW-Sony Upbeat Can Make PS3 Sales Goal," *Reuters UK*, July 12, 2007 (<http://investing.reuters.co.uk/news/articleinvesting.aspx?type=media&storyID=nN12219451>).
- ³ Source: Forrester's North American Consumer Technology Adoption Study Q4 2006 Survey, which surveyed consumers about television-related topics. The verbatim question on HD cable services read: "This question is about HDTV cable and satellite service. You can tell if you have HDTV cable or satellite service if: 1) You receive two versions of channels like CBS, Discovery, and ESPN — one regular and one in HDTV, and 2) when watching an HDTV channel, the TV picture fills the full width of your wide-screen TV without stretching. Do you receive and pay for HDTV cable or satellite service?"
- ⁴ This consumer data comes from Q4 2006, which presents a challenge — it predates widespread release of the PS3, and thus under-represents penetration of Blu-ray players. A second data challenge comes when measuring awareness: The name "HD-DVD" could in fact elicit false positives in terms of consumer awareness, since it parlays closely with "HDTV." The main value of the data is to show that a large number of consumers are under-exposed to both formats, however.
- ⁵ As of August 2007, buyers of HD-DVD players could receive five free discs with their purchase. Buyers of the \$179 Xbox 360 HD-DVD add-on could receive eight free discs. Toshiba's basic HD-DVD player retailed for \$238.88 on Amazon.com, compared with \$448.88 for the least expensive Samsung and \$473.99 for the cheapest Sony Blu-ray players.
- ⁶ Blu-ray enjoys exclusive support from Sony, Disney, Fox, and Lionsgate. Warner Bros. releases films on both formats. Steven Spielberg's films are not included in the Paramount deal, allowing him to release films in either format. Source: Brooks Barnes, "Two Studios to Support HD DVD Over Rival," *The New York Times*, August 21, 2007 (<http://www.nytimes.com/2007/08/21/technology/21disney.html?pagewanted=print>).

- ⁷ The Paramount HD-DVD deal is reportedly only an 18-month arrangement, meaning the studio could move back to Blu-ray releases in 2009 if the winds should shift. Source: Brooks Barnes, "Two Studios to Support HD DVD Over Rival," *The New York Times*, August 21, 2007 (<http://www.nytimes.com/2007/08/21/technology/21disney.html?pagewanted=print>).
- ⁸ Consumers who purchase a new Blu-ray disc player can receive five free Blu-ray discs. Source: Blu-ray.com (<http://www.blu-ray.com/news/?id=280>). Previously, this sort of promotion had been a practice of the HD-DVD Association alone; the Blu-ray camp has realized that promotion is a critical tool in the format war.
- ⁹ Disney is a key backer of Blu-ray, though in the past it has not ruled out the possibility of offering both formats. Source: Ken Fisher, "Disney Considering HD DVD Support, Sees Blu-ray as Eventual Winner," *Ars Technica: The Art of Technology*, March 13, 2006 (<http://arstechnica.com/news.ars/post/20060313-6374.html>). But the summer 2007 Blu-ray push features flashy Disney Blu-ray kiosks in a variety of shopping mall locations. Source: Thomas K. Arnold, "Disney hits the road to shine a light on Blu-ray," *USA Today*, July 16, 2007 (http://www.usatoday.com/life/movies/news/2007-07-16-disney-blu-ray_N.htm?csp=34). While HD-DVD has also enacted road shows, the diversity, number, and brand capital of the Blu-ray Association's membership better positions Blu-ray for these kinds of promotions *en masse*.
- ¹⁰ The BDP-S300 is the cheaper cousin of Sony's flagship \$799 BDP-S1. Source: SonyStyle.com (<http://www.sonystyle.com/webapp/wcs/stores/servlet/CategoryDisplay?catalogId=10551&storeId=10151&langId=-1&categoryId=27898>). The 60-Gigabyte version of the PS3 now sells for \$499 in the United States. Source: Michael White, "Sony cuts PlayStation 3 price in U.S.," *International Herald Tribune*, July 9, 2007 (<http://www.iht.com/articles/2007/07/09/business/sxsony.php>).
- ¹¹ HD-DVD players are certainly poised to enter this range by the latter half of 2007. The first sub-\$200 HD-DVD player should be available to consumers by the holiday season. Source: "Venturer HD DVD Player to Ship in Time for 2007 Holiday Sales," August 28, 2007 (<http://www.venturer.com/news-details.aspx?id=15>).
- ¹² Some of the newer titles, and the release of the television series "Prison Break" on Blu-ray disc, should help the Blu-ray cause, however. Source: "Fox and MGM Unveil Blu-ray Exclusives," August 20, 2007 (<http://www.comingsoon.net/news/movienews.php?id=36494>).
- ¹³ Blockbuster will carry Blu-ray, but not HD-DVD, in 1,700 of its retail locations. Source: "Blockbuster to Expand Blu-Ray to 1,700 Stores," Blockbuster press release, June 18, 2007 (<http://www.b2i.us/profiles/investor/ResLibraryView.asp?BzID=553&ResLibraryID=20345&Category=1027>).

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